West Yorkshire Combined Authority

LEEDS CITY REGION ENTERPRISE PARTNERSHIP

ECONOMIC AND BREXIT MONITOR: LEEDS CITY REGION, SEPTEMBER 2018

Key points at glance

This report presents the latest assessment of the Leeds City Region economy. It sets out the recent developments in the world's leading economies, along with trends and forecasts for global growth. It analyses the recent economic performance of the UK, before considering in more detail the latest developments in Leeds City Region.

National and international headlines

- The global outlook has become more mixed in recent months, as concerns over trade wars and tariffs pose a risk to recent solid performance for some nations and regions.
- US GDP increased by 1% in Q2 2018, its fastest expansion since 2014. Growth slowed in the EU and China but remained positive.
- UK GDP increased by 0.4% Q2, compared to the previous three months. This is up from growth of 0.2% in Q1.
- UK productivity decreased by 0.4% in Q1 2018. Output per hour is 0.9% higher than a year earlier but this remains below the long term pre-recession trend of 2% growth.
- The UK employment picture remains strong, with 388,000 more people are in work than a year ago. The employment rate has risen to a new record high of 75.7%.
- The unemployment rate has also fallen, to 4.2% down from 4.5% a year ago.
- Average earnings increased by 2.7% in the three months to May, a slight slowdown on the preceding three months, but still outpacing inflation which has remained steady at 2.4%.
- The Bank of England has increased interest rates to 0.75%, their highest level in almost a decade in response to strong labour market conditions and signs of economic improvement.

Key City Region and local developments

- There was a slight slowdown in private sector growth across the Yorkshire & Humber region in June, according to the Natwest/Markit regional PMI.
- Whilst optimism was higher than most other UK regions, it was still at a 22 month low.
- Goods worth a total of £4.34bn were exported from Yorkshire & Humber in Q1 2018, down only slightly from the record £4.39bn seen in Q4 2017. The value of the region's goods exports was 2.9% higher than the same period last year, broadly in line with the 2.7% growth seen nationally.
- The number of City Region residents in work was largely unchanged from the previous quarter according to the ONS Annual Population Survey. 5,000 more people are in work than a year ago, an increase of 0.4%.
- The employment rate for Leeds City Region is 73.5%, again broadly unchanged from Q4 2017.
- House prices in Yorkshire & Humber increased by 2.9% in the year to May 2018, up from 2.7% in the year to April. Price growth is similar to the UK, where prices were up 3% in May.
- Average rents for West Yorkshire office space dipped slightly in Q2 2018, from £14 per square foot to £13.8 according to CoStar. West Yorkshire has seen relatively stable office rents compared to these markets in recent years and prices are therefore more affordable here, albeit higher than in other major city regions.

Brexit implications and conclusions

- As with other regions, businesses in Yorkshire and Humber continue to see cost pressures from sterling's post-Brexit fall, as well as issues such as higher oil prices and wages. Conversely, the weak pound has undoubtedly been beneficial to exporters, though there are indications this growth has levelled off.
- The City Region has seen slightly lower employment growth in the past year than the nation as a whole. Overall however, employment levels remain strong and unemployment below historical averages. Higher growth in other city regions may reflect higher levels of slack in those labour markets.
- Relatively stable commercial property prices may be indicative of wider hesitancy and risk aversion in the economy, as businesses delay investment decisions in the absence of greater clarity. Rents here remain more affordable than other major cities, which may make the area more attractive in a risk-off environment, particularly to SMEs.

These issues are explored in greater detail in the remainder of this document.

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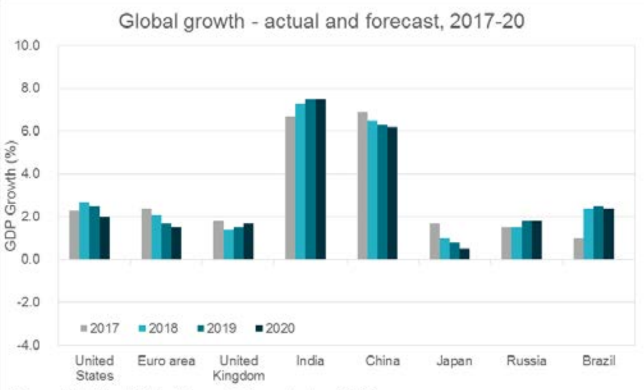
ECONOMIC AND BREXIT MONITOR: LEEDS CITY REGION, SEPTEMBER 2018

Introduction

- This report presents the latest assessment of the Leeds City Region economy. It sets out the recent developments in the world's leading economies, along with trends and forecasts for global growth. It analyses the recent economic performance of the UK, before considering in more detail the latest developments in Leeds City Region.
- New data available includes updated global economic forecasts from the World Bank, whilst new official UK data is available on GDP for Q2 2018 and the labour market up to May 2018. There is also new official data on trade, inflation and consumer spending.
- For Leeds City Region, labour market for Q1 2018 and regional goods exports data from HMRC for the same period are also presented along with data from Banksearch on the number of new business bank accounts for Q2 2018.

Global economic and political developments



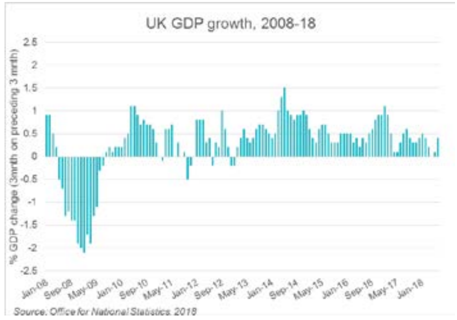
Source: World Bank Global Economic Prospects, June 2018

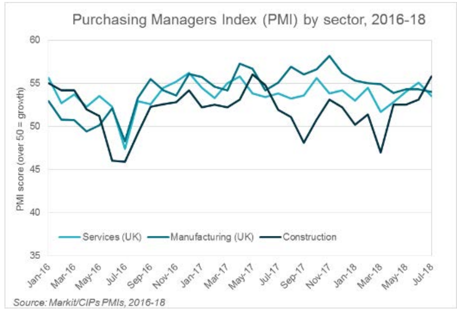
- The global outlook has become more mixed in recent months, as concerns over trade wars and tariffs pose a risk to recent solid performance for some nations and regions.
- Growth accelerated in the US, with GDP up by 1% in Q2 2018 compared to growth of 0.6% in the previous quarter. Recent tax changes have driven consumer spending, whilst strong exports also contributed to the fastest growth seen since 2014.
- Eurozone GDP increased by 0.3% in Q2 2018, down slightly from 0.4% in Q1. Concerns over trade wars and weaker confidence among appear to be subduing demand.
- Growth in China also slowed slightly in Q2, though so far the 2nd largest economy remains relatively unaffected by tariffs imposed on exports to the US. Export growth for China accelerated in June, whilst domestic demand also remains strong.
- Oil prices remain around a three year high of $75 a barrel following the re-imposition of sanctions on Iran.
- The World Bank expects global growth to remain at 2017 levels this year, before tailing off as the recovery in emerging markets levels off. However, the World Bank remain cautious about the risks that trade protectionism and volatility in financial markets pose, particularly to emerging economies.
- The World Bank expect UK growth to slow from 1.8% last year to 1.4% in 2018, before recovering to 1.5% and 1.7% in the subsequent two years.
- The Bank of England have increased the base interest rate to 0.75% - its highest level in almost a decade. The Bank cited an upturn in momentum in the UK economy, as well as the lack of slack in the labour market which it expects to lead to higher wage growth in the coming months, as justification that the economy could withstand an increase.
- The Bank did however note that their assumptions were based on a relatively smooth exit from the European Union. Governor Mark Carney commented that whilst a "no deal" Brexit was relatively unlikely, it would be "highly undesirable" as the supply chain impacts would push up consumer prices.
- That echoes views expressed by leaders at some of the UK's largest companies. Airbus have said a disorderly exit could lead them to halt production, and they have begun to stockpile parts in an attempt to mitigate this risk. The CEO of Rolls Royce has suggested they may do the same towards the end of this year, whilst they are also having conversations with smaller suppliers to understand risks in more detail.
- Jaguar Landrover meanwhile have said a "bad Brexit deal" could cost them £1.2bn a year in profit, and would put plans to invest £80bn over the next five years at risk.

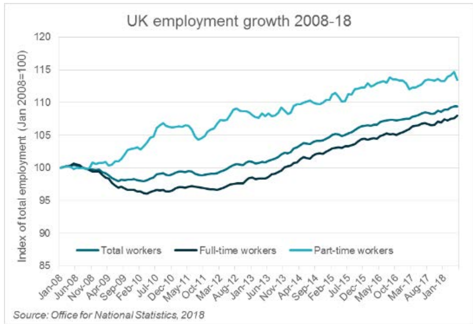
Global economy summary: The global outlook has become more mixed as concerns over trade wars and tariffs pose a risk to recent solid performance for some nations and regions. However, the rise in UK interest rates reflects the nation's strong labour market and recent signs of an economic upturn. The range of voices warning of the challenges that a disorderly EU exit would bring emphasises the risks that remain.

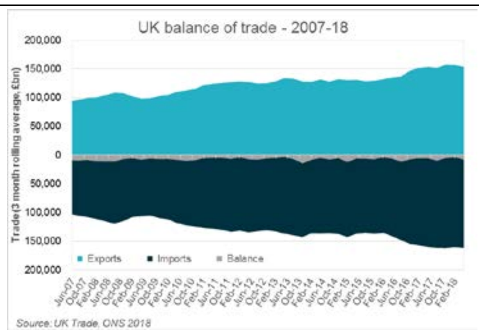
UK economic dashboard

<table>
<tr><th>Indicator</th><th>Latest position</th><th>Chart</th><th>Trend</th></tr>
<tr><td>Economic headlines</td><td>UK GDP increased by 0.4% Q2, compared to the previous three months. This is up from growth of 0.2% in Q1. Growth was strongest at the start of the quarter, but slowed to 0.1% in June. Construction output increased by 0.9% over the quarter, with services output up 0.5%. This was offset by a 0.8% fall in production.

UK productivity decreased by 0.4% in Q1 2018. It is 0.9% higher than a year earlier, below the pre-recession growth rate of 2%.</td><td>
</td><td></td></tr>
<tr><td>Confidence and sentiment</td><td>Construction output accelerated in July, according to Markit/CIPS, with housebuilding and commercial activity growing at its fastest pace in over two years. Despite solid expansion, sentiment was subdued among construction and manufacturing firms, with both citing Brexit uncertainty.

Expansion slowed in the service sector, with respondents noting more risk-aversion and delays in decision making due to Brexit.</td><td>
</td><td></td></tr>
<tr><td>Labour market</td><td>Total employment in the UK increased by 137,000 to 32.4 million in the three months to May 2018, according to ONS. 388,000 more people are in work than a year ago. The employment rate has risen to a new record high of 75.7%.

Unemployment fell in the three months to May, down 12,000 to 1.41 million. The unemployment rate of 4.2% is down from 4.5% a year ago.</td><td>
</td><td></td></tr>
<tr><td>Trade and exports</td><td>Good weather and the football World Cup helped retail sales to increase by 2.1% in the three months to June, their fastest pace since 2015.

The UK's trade deficit increased by £5bn to £8.3bn in the three months to May, thanks to a fall in goods exports and a rise in goods imports.</td><td>
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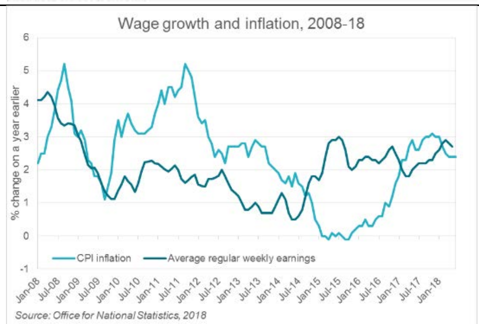
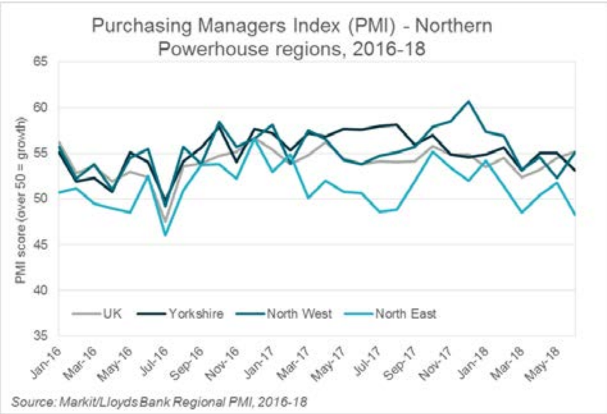
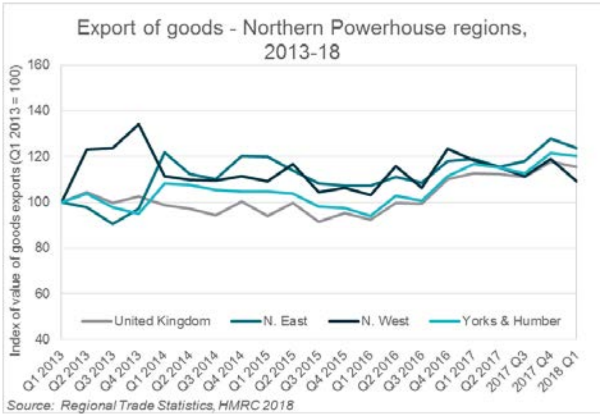
<tr><td>Inflation and wages</td><td>Inflation held steady at 2.4% in June, unchanged for the third consecutive month. Higher fuel costs were a key driver of inflation, though this was offset by falling clothing prices.

Average earnings increased by 2.7% in the three months to May, compared to a year ago, similar to growth of 2.8% in the preceding three months. Pay increased by 0.2% in real terms over this period. Adjusted for inflation however, total pay is £33 per week lower than in 2008.</td><td>
</td><td></td></tr>
<tr><td colspan="4">Brexit implications: UK growth remains on a par with late 2017 but below longer term growth rates, with business surveys pointing to Brexit as a key factor weighing on business confidence. This appears to be leading to lower or delayed investment, which will have implications for productivity growth and competitiveness. The labour market remains strong however, perhaps as businesses offset capital investment with more readily available labour. This is unlikely to remain feasible forever, with employment at record highs and some surveys suggesting companies are finding it increasingly difficult to find skilled workers.</td></tr>
</table>

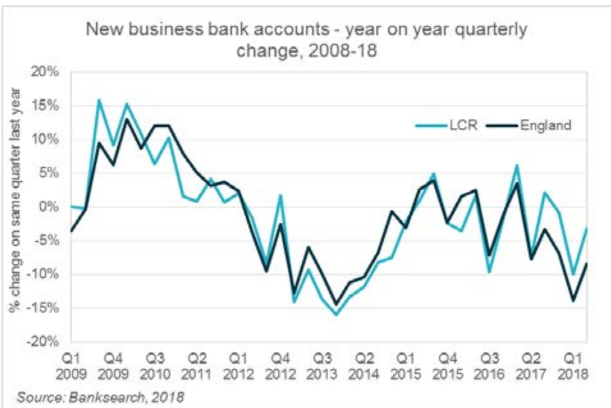
Leeds City Region – Business Performance and Trade

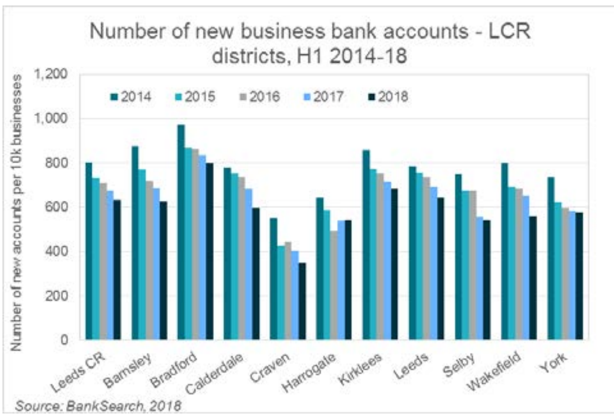
- There was a slight slowdown in private sector growth across the Yorkshire & Humber region in June, according to the Natwest/Markit regional PMI. The headline measure of business activity dipped to 53.1 in June, down from 55 in May and below the UK level of 55.2 (a reading of over 50 indicates growth).
- A combination of factors have led to increasing price pressures for Yorkshire businesses according to Markit, including raw material costs, wage growth and the weakness of sterling. Whilst optimism was higher than most other UK regions, it was still at a 22 month low.
- Goods worth a total of £4.34bn were exported from Yorkshire & Humber in Q1 2018, down only slightly from the record £4.39bn seen in Q4 2017. The value of the region's goods exports was 2.9% higher than the same period last year, broadly in line with the 2.7% growth seen nationally. Among other northern regions, the North East saw a 4% increase compared to last year, though the value of goods exports from the North West declined by 7.8%.
- The European Union accounted for 61.6% of goods exports from Yorkshire & Humber in Q1 2018, higher than the 58% averaged across 2017. North America and Asia/Oceania accounted for 11% each.





- Just over 4,000 new business bank accounts were opened in Leeds City Region in Q1 2018 according to BankSearch, an almost identical number to Q1. The number of new accounts opened is 3.1% lower than Q2 2017, a smaller fall than the 8.4% fall seen nationally ranking Leeds City Region 11th out of 38 LEPs so far in 2018.
- Bradford has seen the highest number of new business bank accounts per 10,000 existing businesses so far this year, with 798 new accounts per 10,000. Kirklees has the 2nd highest rate at 681 businesses.
- Harrogate remains the only district of Leeds City Region to have seen an increase in the rate of new business bank accounts so far this year, with the number of new openings up 0.4%.

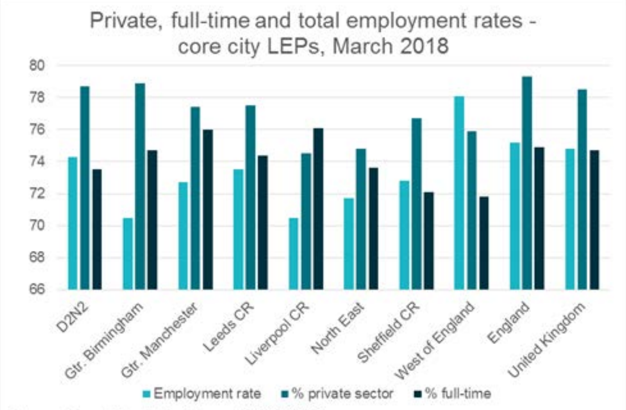




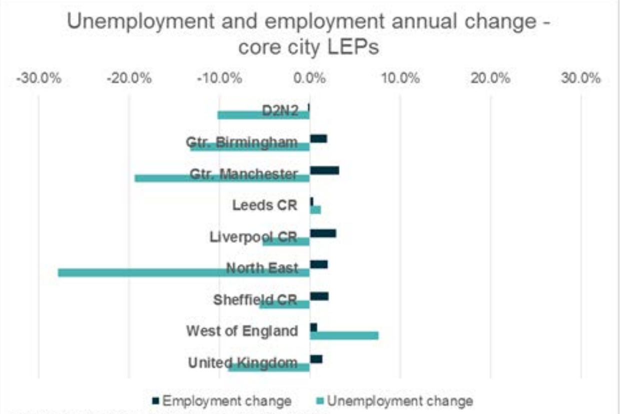
Brexit implications: As with other regions, businesses in Yorkshire and Humber continue to see cost pressures from sterling's post-Brexit fall, as well as issues such as higher oil prices and wages. Conversely, the weak pound has undoubtedly been beneficial to exporters, though there are indications this growth has levelled off. Brexit was cited as a key cause of the fall in business optimism in the Yorkshire & Humber June PMI survey, though concerns over trade wars and tariffs were also raised. New business formation appears to be slightly below 2017 levels, perhaps indicative of lower confidence and sentiment.	

Leeds City Region – Labour Market

- There were 1.41 million Leeds City Region residents in work in Q1 2018, largely unchanged from the previous quarter according to the ONS Annual Population Survey. 5,000 more people are in work than a year ago, an increase of 0.4%.
- Employment increased at a slower rate than most core city LEPs, though D2N2 saw employment decline by 0.2% over the past year. Greater Manchester (+3.2%) and Liverpool City Region (+2.9%) saw the fastest increases. Employment growth in most core city districts outpaced that of the respective LEP.
- Employment in Leeds increased by 3.8% over the past year, slightly above the average for all core cities (3.4%). Manchester saw the fastest growth (10.1%), followed by Newcastle (4.7%) and Liverpool (3.9%).



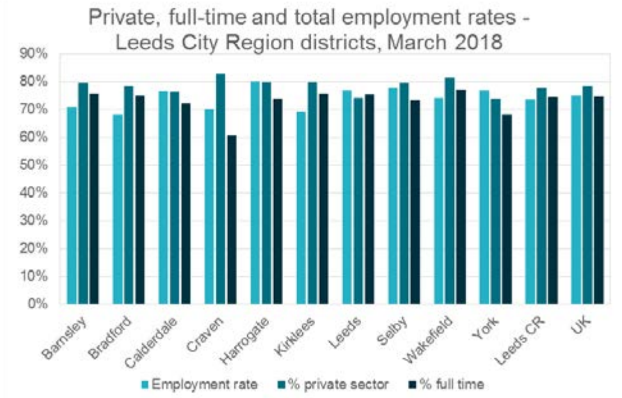
Source: Annual Population Survey, NOMIS, 2018



Source: Annual Population Survey, NOMIS, 2018

- The employment rate for Leeds City Region is 73.5%, broadly unchanged from Q4 2017. Whilst most core city LEPs have seen their employment rates increase of late, the rate in Leeds City Region remains third highest among core city LEPs and higher than other northern core cities.
- The proportion of Leeds City Region residents working full-time fell slightly over the past quarter, from 75% to 74.4%. The proportion of workers employed in the private sector remained at around 77.5%. The City Region performs relatively well against northern core city LEPs on private sector employment, though it has relatively lower levels of full-time workers compared to Greater Manchester and Liverpool City Region.
- There is a mixed picture at district level at the start of 2018. York (+3.2%) and Leeds (+1%) have both seen employment increase between Q4 2017 and Q1 2018. Kirklees (-1.6%) and Craven (-3.4%) have seen employment fall, though data can fluctuate for smaller geographies. Other districts have been largely flat.
- The employment rate in York increased by over 2% to 76.9%, taking it above the national average of 74.8%. Leeds (76.8%) and Calderdale (76.6%) also saw the rate increase. It also remains above the national average in Harrogate (80%) and Selby (77.7%).

Source: Annual Population Survey, NOMIS, 2018



Source: Annual Population Survey, NOMIS, 2018

- Unemployment increased in Calderdale, Kirklees and York in Q1, but this was more than offset by falling unemployment in Bradford and Leeds. Total unemployment in the City Region fell by 1,800 to 68,300 – a fall of 2.8%. All core city LEPs saw unemployment fall over this period, most to a similar extent to LCR.
- The City Region unemployment rate of 4.6% is close to the UK average of 4.4%, and below core city LEPs except West of England (3.9%) and D2N2 (3.8%). York (3.2%), Calderdale (3.9%) and Leeds (4%) all have unemployment rates below the UK average.

Brexit implications: The City Region has seen slightly lower employment growth in the past year than the nation as a whole. Overall however, employment levels remain strong and unemployment below historical averages. Higher growth in other city regions may reflect higher levels of slack in those labour markets.

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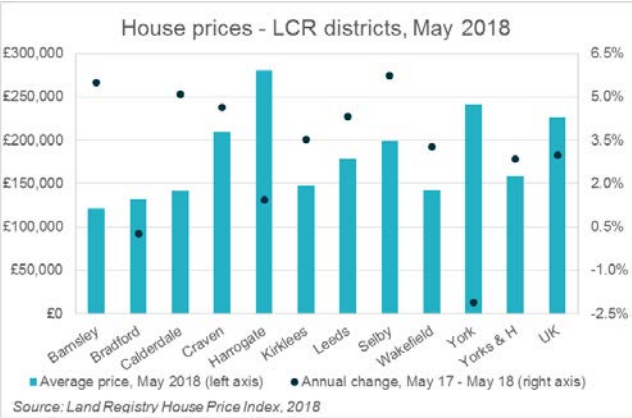
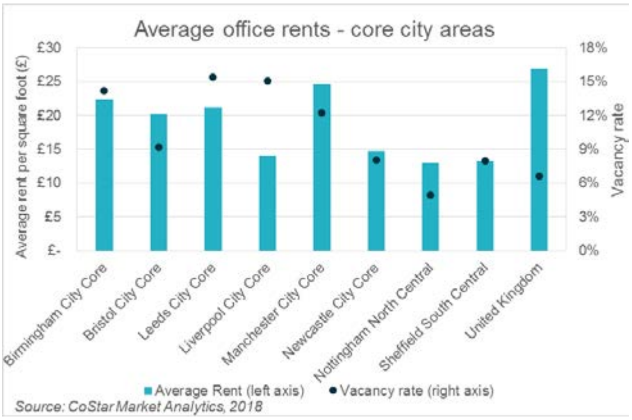
LEEDS CITY REGION ENTERPRISE PARTNERSHIP

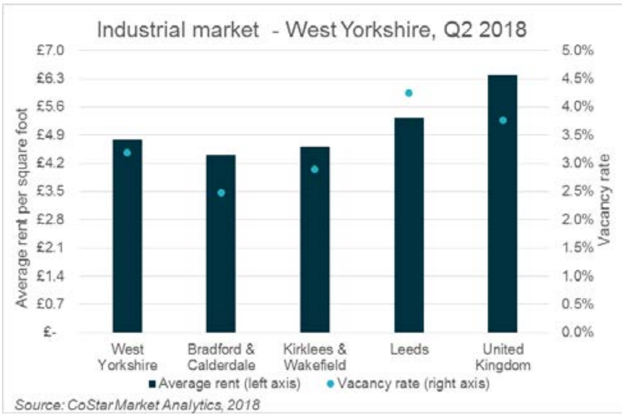
Leeds City Region – Housing, Property and Infrastructure

- House prices in Yorkshire & Humber increased by 2.9% in the year to May 2018, up from 2.7% in the year to April. Price growth is similar to the UK, where prices were up 3% in May.
- Price growth was slightly stronger in West Yorkshire, where average prices were up 3.2%. Increases in Calderdale (5.1%) and Leeds (4.3%) contributed to this. Across the wider City Region, Selby (+5.7%) saw the fastest growth, though prices declined by 2.1% in York.
- Most districts of the City Region have average house prices below the UK average of £226,000, though prices in Harrogate (£280,000) and Yorkshire (£241,000) exceed this. Prices are lowest in Barnsley (£122,000) and Bradford (£132,000).



- Home ownership in Leeds City Region remains relatively more affordable than across England as a whole. The average house across England costs 7.9 times average earnings at the end of 2017, up from 7.7 a year earlier and 7.1 in 2017. The ratio has remained more stable in Leeds City Region, increasing from 5.8 in 2014 to 6.1 in 2017.
- The affordability ratio in Leeds City Region is similar to Greater Manchester and D2N2 (both 5.9) and lower than Greater Birmingham (6.7) and West of England (9). The Sheffield and Liverpool City Region both have lower affordability ratios, as does North East LEP area.





- Average rents for West Yorkshire office space dipped slightly in Q2 2018, from £14 per square foot to £13.8 according to CoStar. Rents were flat in Birmingham over this period, whilst Manchester saw an increase of 0.7%. West Yorkshire has seen relatively stable office rents compared to these markets in recent years and prices are therefore more affordable here, albeit higher than in other major city regions.
- The picture is similar when looking at city centre rents, with prices in Leeds (£21.2/sf) being a little below Birmingham (£22.4) and Manchester (£24.7).
- Elsewhere in the City Region, office rents are much lower than in Leeds at around £10/sf in Bradford, Kirklees and Calderdale and £11/sf in Wakefield.
- There is less variation in rents for industrial space across West Yorkshire, with rents in all areas below the UK average of £6.4/sf. Rents in Leeds are £5.3/sf, compared to around £4.5/sf elsewhere. The vacancy rate in Leeds is also slightly above national average, whilst there is less slack elsewhere in the county.

Brexit implications: Relatively stable commercial property prices may be indicative of wider hesitancy and risk aversion in the economy, as businesses delay investment decisions in the absence of greater clarity. Rents here remain more affordable than other major cities, which may make the area more attractive in a risk-off environment, particularly to SMEs.

Conclusions and outlook

- A range of factors have led to a more mixed outlook for the global economy. The prospects of a trade war have increased with the imposition of tariffs on trade between the US, China and the EU. The former two appear to have been relatively unaffected to date, with domestic demand sustaining strong growth and exports remaining strong. Major EU exporting nations such as Germany also do not appear to have been greatly affected so far, though surveys suggest the issue is weighing on business confidence and the outlook for coming months.

- Other geopolitical factors such as the re-imposition of sanctions on Iran are also serving to push up costs for some businesses. This is particularly an issue for the UK, where businesses are already contending with price pressures from the fall in sterling. These issues appear to be contributing to a less confident outlook for UK businesses, and indeed those in our region.

- Brexit however appears increasingly central to the thinking of many businesses as the March date for the UK to leave the EU approaches with many issues unresolved. There are signs that this is increasing difficulties with finding workers, with the Chartered Institute of Personal Development (CIPD) suggesting that falling EU migration has led to skills shortages. The CIPD's surveys suggest the number of applicants per vacancy fell from 24 to 20 for low skilled vacancies, and from 19 to 10 for mid-skilled jobs. Around half of respondents had increased starting salaries in response.

- Whilst wage growth remains relatively subdued in real terms, the positive employment picture and expectations of wage growth was partly behind the Bank of England's decision to increase interest rates to their highest level since 2009. Whilst the outlook for the UK economy remains mixed, a rebound in growth in Q2 gave the Bank the confidence to raise rates whilst also acknowledging that the future path remains uncertain.

- Brexit is the key source of that uncertainty, with surveys suggesting that it is having an impact on investment as companies delay decisions until they have greater clarity.

- That appears to apply equally to firms in Yorkshire, who despite still being more confident than counterparts elsewhere in the country, have seen confidence levels fall in recent months. Despite this, survey data continues to reflect a largely positive view of activity across Yorkshire with businesses more optimistic than in all regions except the East Midlands in June.

- This is not borne out some official data which shows that employment growth in the City Region remains relatively subdued compared to some other city regions. Indeed, this suggests a wider issue across Yorkshire and Humber, where employment growth of 0.2% was below the 0.6% seen nationally.

- It is however notable that major cities appear to be the drivers of jobs growth of late, both locally with York and Leeds seeing the fastest growth so far this year, and nationally with other core cities leading jobs growth in their respective City Regions.

- Slightly lower employment growth here also perhaps reflects the fact that the employment rate in the Leeds City Region is already higher than most other core city regions, so there is less slack in the local labour market and more scope for faster employment growth in other City Regions. If that is the case, it re-emphasises the importance of accelerating productivity growth to drive future expansion and prosperity. The challenge in achieving this is emphasised by the fact that UK productivity continues to show little improvement, despite the apparent lack of slack in the labour market.

- It may also be that other indicators are more prevalent in business' minds at present, with export performance still strong even if there are signs that recent growth levels may have levelled off. Whilst it is clear that Brexit poses a number of challenges that appear to be of increasing concern to businesses, it is equally clear that exporters have taken advantage of beneficial trading conditions. This may remain the case for the months ahead, with the pound likely to remain subdued until the UK's future relationship with the EU becomes clearer.

This briefing has been produced by the West Yorkshire Combined Authority Research & Intelligence team. Any comments or queries can be addressed to research@westyorks-ca.gov.uk.